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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1941

No. 1086 61

In the Matter
of

THE WESTERN PACIFIC RAILROAD COMPANY,
a corporation,

Debtor.

IRVING TRUST COMPANY, as Substituted Trustee under the
General and Refunding Mortgage of The Western Pacific Railroad
Company,

Petitioner,

against

CROCKER FIRST NATIONAL BANK OF SAN FRANCISCO
and SAMUEL ARMSTRONG, as Trustees under The Western
Pacific Railroad Company First Mortgage dated June 26, 1916;
FREDERICK H. ECKER, JOHN W. STEDMAN and REEVE
SCHLEY, constituting the Institutional Bondholders Committee;
WESTERN PACIFIC RAILROAD CORPORATION; THE
WESTERN PACIFIC RAILROAD COMPANY; A. C. JAMES
CO.; THE RAILROAD CREDIT CORPORATION; and RE-
CONSTRUCTION FINANCE CORPORATION,

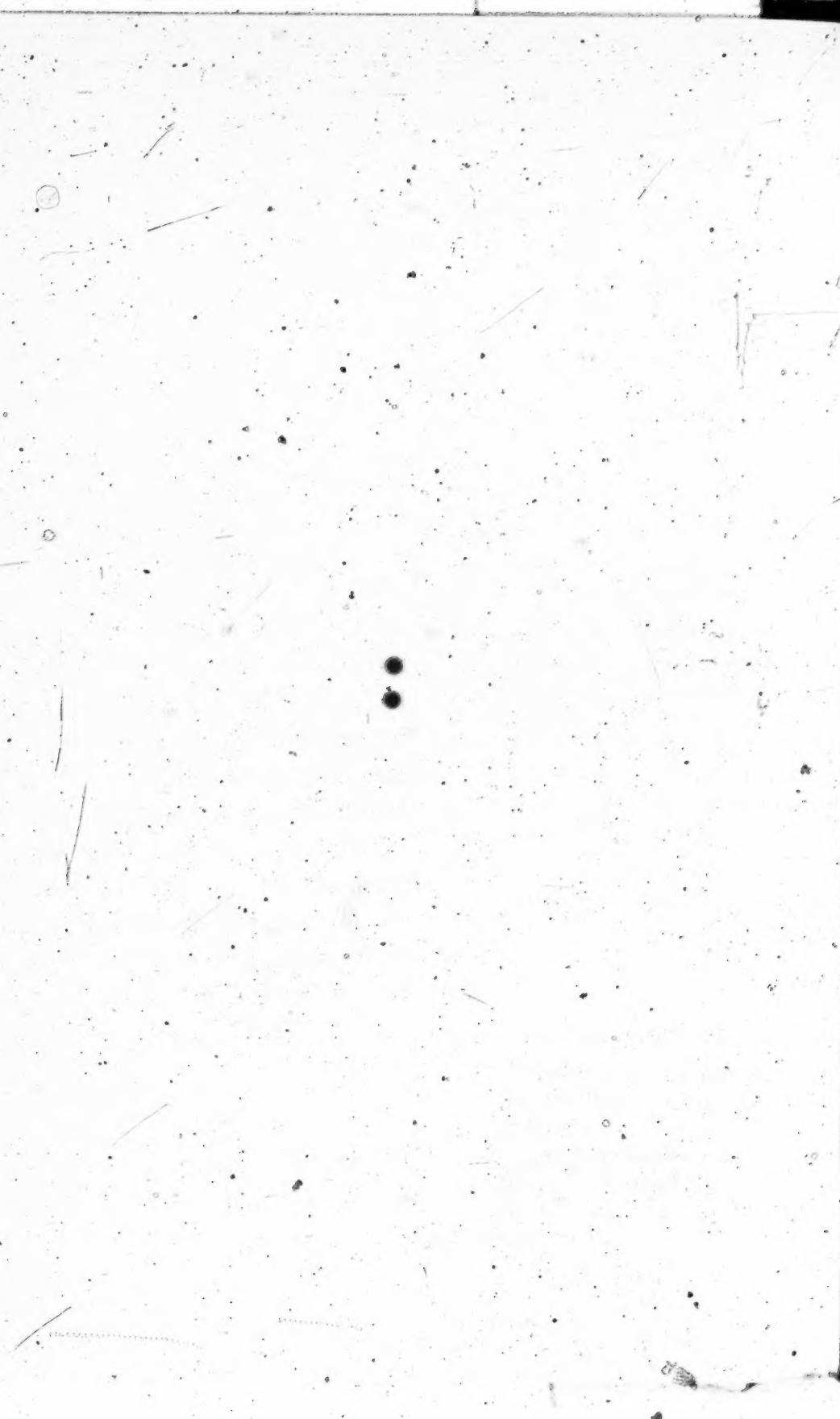
Respondents.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit

HAROLD C. MCCOLLOM,
Attorney for Petitioner

ORRIN G. JUDD,
Of Counsel.

Dated, New York, March 28, 1942.



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CROCKER FIRST NATIONAL BANK OF SAN FRANCISCO and
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Pacific Railroad Company First Mortgage dated June 26,
1916; FREDERICK H. ECKER, JOHN W. STEDMAN and REEVE
SCHLEY, constituting the Institutional Bondholders Com-
mittee; WESTERN PACIFIC RAILROAD CORPORATION; THE
WESTERN PACIFIC RAILROAD COMPANY; A. C. JAMES CO.;
THE RAILROAD CREDIT CORPORATION; and RECONSTRUCTION
FINANCE CORPORATION,

Respondents.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit

To the Honorable the Chief Justice and the Associate
Justices of the Supreme Court of the United States:

Your petitioner, Irving Trust Company, as Substituted
Trustee under the General and Refunding Mortgage of
The Western Pacific Railroad Company, dated as of Janu-

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ary 1, 1932 (hereinafter respectively called the "Refunding Mortgage Trustee" and the "Refunding Mortgage"), respectfully prays for a writ of certiorari to review a decision of the United States Circuit Court of Appeals for the Ninth Circuit, rendered February 16, 1942 (R. 2681), on rehearing, of an earlier decree of said Court dated November 28, 1941 (R. 2663, 2675), which reversed an order of the United States District Court for the Northern District of California, entered August 15, 1940 (R. 2569), approving a plan of reorganization for the Debtor under Section 77 of the Bankruptcy Act.

The review sought by this petition is limited to the questions concerning the relative liens of the Refunding Mortgage and the so-called First Mortgage of the Debtor. Petitions for writs of certiorari to review said decree of November 28, 1941 in other respects are already pending, having been filed respectively by Frederick H. Ecker, *et al.* (No. 819), and Crocker First National Bank of San Francisco, *et al.* (No. 820).

The record on this petition is the same as the record on No. 819 (which constitutes the record on No. 820 also). This petitioner begs leave to refer to the certified transcript filed in No. 819, and prays that such certified transcript be deemed to accompany this petition within the meaning of Rule 38 of this Court.

Opinions below.

The opinion of the District Court, dated August 15, 1940 (R. 1569), is reported in 34 F. Supp. 493.

The opinion of the Circuit Court of Appeals, dated November 28, 1941 (R. 2663), is reported in 124 F. (2d) 136.

No opinion was rendered by the Circuit Court of Appeals in deciding the petitions for rehearing. The order thereon dated February 16, 1942, amending a prior order dated February 12, 1942, is printed in the supplemental record (R. 2681).

Jurisdiction

The jurisdiction of this Court is invoked under Section 240-a of the Judicial Code, as amended by Act of Congress of February 13, 1935 (U. S. Code, Title 28, Section 347-a).

Petitioner's time to apply for certiorari runs from the date of the Circuit Court of Appeals' decision on rehearing, namely, three months from February 16, 1942. *Chicago Great Western R. Co. v. Basham*, 249 U. S. 164; *Robertson, Practice & Procedure in the Supreme Court of the United States* (Rev. Ed. 1929), p. 4.

Statement of the matters involved

Petitioner, Irving Trust Company, was substituted as Trustee under Debtor's Refunding Mortgage on November 13, 1936 (R. 1053) during the course of hearings before the Interstate Commerce Commission on various proposed plans of reorganization. Bonds outstanding under the Refunding Mortgage aggregate \$18,999,500 principal amount (R. 1056), and all of them are pledged, in varying amounts, with three creditors, namely, A. C. James Company, Railroad Credit Corporation, and Reconstruction Finance Corporation.

The Refunding Mortgage is a lien on substantially all the property of the Debtor (R. 1231-46).* The lien of

* The granting clauses of the Refunding Mortgage are printed in the record at the pages indicated. The balance of the Mortgage (I.C.C. Ex. 6) is not printed, but constitutes part of the record, under a stipulation approved by the Circuit Court of Appeals (R. 2612-25).

the Refunding Mortgage is subject "in so far, but only in so far (in extent, degree of priority or otherwise), as in law the same respectively may attach" (R. 1245) to the First Mortgage of the Debtor dated June 26, 1916, under which there are outstanding approximately \$50,000,000 principal amount of bonds (R. 1047).

Evidence respecting the relative lien of the two mortgages on various parcels of property was introduced before the Interstate Commerce Commission. The Commission, while stating that "final adjudication of this and similar questions must be made by the court" (R. 262), made a preliminary determination, overruled the Refunding Mortgage Trustee's contentions and stated that the First Mortgage bondholders should be "considered as having a first lien upon practically all the assets of the Debtor" (R. 267). In consequence, its original Report provided for the issuance of nothing but common stock to the creditors secured by Refunding Mortgage bonds (R. 278) in respect of the security afforded by such bonds.

Following a petition for modification filed by the Refunding Mortgage Trustee, the Commission, in a supplemental report, recognized that deposited cash and certain securities of Tidewater Southern Railway Company, which were admittedly subject to the Refunding Mortgage as a first lien, had substantial value, and directed that the holders of Refunding Mortgage bonds be awarded, in consideration thereof, new income mortgage bonds in the amount of \$732,010, and new participating preferred stock of a par value of \$1,147,955 (R. 315).

The Refunding Mortgage Trustee, filed objections to the approval of the Plan, which were overruled by the District Court (R. 1597).

Thereafter, the Refunding Mortgage Trustee appealed to the Circuit Court of Appeals from the order approving the Plan. The appeal was limited (R. 1616, 1651) to questions relating to the lien of the Refunding Mortgage, in respect of which the pledgees of the Refunding Mortgage bonds have recognized that the Refunding Mortgage Trustee was the appropriate party to present such questions (R. 911, 961, 1631, 1644; I.C.C. Min. 477, 550-51). The present petition is filed at the express request of two of such bondholders.

Proceedings in the Circuit Court of Appeals

The opinion of the Circuit Court of Appeals did not deal with the legal questions of conflicting lien, and made no determination with respect thereto. In its original opinion, the Circuit Court of Appeals ruled that the Refunding Mortgage Trustee was not adversely affected by the Plan and was not entitled to appeal, and dismissed its appeal (R. 2668; 124 F. (2d) at 138).

Thereafter the Refunding Mortgage Trustee filed a timely petition for rehearing seeking to have the Circuit Court of Appeals' decision modified so as to determine that the Refunding Mortgage Trustee was a proper party appellant, and so as to include an immediate determination of the lien question.

The Circuit Court of Appeals, on such petition for rehearing, set aside that portion of the decree dismissing the appeal of the Refunding Mortgage Trustee, but denied the petition for other relief (R. 2681).

In other words, the Circuit Court of Appeals has recognized the standing of the Refunding Mortgage Trustee as a proper party appellant, but has declined to decide at this time the questions raised by its appeal with respect to the extent of the lien of the Refunding Mortgage.

One other portion of the Circuit Court of Appeals' original opinion is very pertinent to the claims of the Refunding Mortgage Trustee. The Court, in directing that the Plan be remanded to the Commission, stated that it was necessary for the Commission to make findings with respect to the *value* of

"(1) the property subject to the refunding mortgage only and (2) the property subject both to the refunding mortgage and to the first mortgage." (R. 2670; 124 F. (2d) at 139.)

It will be difficult, to say the least, for the Commission to make such findings until there has been a final determination of the extent of the respective liens of the two mortgages.

The lien questions

Without attempting to argue the merits of the lien controversy in this petition, we set forth below a summary of the facts and legal contentions on each question, so that this Court may have before it both the nature of the items involved and the principal legal issues which are presented with respect to each item.

1. The first issue of lien relates to certain of the Debtor's rolling-stock, which was acquired under conditional sale or equipment-trust agreements, and in which the Debtor had an equity at the date of institution of the proceedings of over \$6,000,000 (R. 1074). All the payments on account of this rolling-stock were made from the Debtor's free funds, or from proceeds of Refunding Mortgage bonds (R. 1073-74). None of it was owned by the Debtor at the time of the execution of the First Mortgage.

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The exclusion from the lien of the First Mortgage of equipment-trust rolling stock bought with free funds is clearly set forth in the granting clause of the First Mortgage, which provides (R. 1229) :

"and the Company may, unless First Mortgage Bonds shall have been authenticated and delivered or their proceeds or other cash deposited hereunder paid out against the same, purchase and acquire equipment, free from the lien hereof, by lease, conditional sale agreement or under any form of equipment trust, or purchase such equipment and issue obligations therefor secured by mortgage or pledge of such equipment superior to the lien of this indenture." (Italics supplied by counsel.)

The Refunding Mortgage contains express provision pledging the equity ~~in~~ such rolling-stock (R. 1244-45).

The reason given by the Commission (R. 266) and adopted by the Court (R. 1597) for nevertheless holding such rolling-stock to be subject to the First Mortgage was an alleged inconsistency between the free funds clause and the subject clause of the First Mortgage, which latter provided (R. 1230) :

"SUBJECT, HOWEVER, as to all equipment now owned to the equipment trust or conditional sale agreements secured thereon, and as to equipment hereafter acquired, to the equipment trust or conditional sale agreements to which the same shall be subject as permitted hereby" (Italics supplied by counsel.)

The fallacy of this argument lies in the failure to consider the first italicized provision of the free funds clause above which, we believe, clearly contemplates that rolling-stock may be acquired under equipment-trust either (1)

with First Mortgage funds—in which event the First Mortgage will be a lien thereon “subject . . . to the equipment trust or conditional sale agreements . . . permitted hereby”, or (2) with free funds—in which event the equipment will be “free from the lien hereof”.

2. The second lien question relates to the Debtor's Northern California Extension. This extension was completed in 1932, at a cost of over \$10,000,000 (R. 1078), and has proved to be one of the most valuable parts of the Debtor's system (R. 1935, 1942-48, 1980). The Refunding Mortgage Trustee claims that the Extension is subject to the lien of the First Mortgage only to the extent of the First Mortgage bonds (\$5,000,000 principal amount) used in the construction thereof and that otherwise it is subject, under the facts appearing in the record, to the *pari passu* lien of the Refunding Mortgage, inasmuch as the moneys for the completion of the Extension (over \$5,000,000) were supplied by the Refunding Mortgage creditors (R. 1078; I.C.C. Ex. 52, p. 647), and less than half the cost of land on which it is built was paid from First Mortgage funds (R. 1082-84).

The extension is specifically described in the Refunding Mortgage (R. 1236).

No supplemental indenture was ever executed subjecting the Extension to the lien of the First Mortgage (R. 1077). It cannot be brought under the after-acquired property clauses as an appurtenance of the mortgaged property (*New Orleans Pacific R. Co. v. Parker*, 143 U. S. 42, 55; *Humphreys v. McKissock*, 140 U. S. 304, 313-14).

The holding that the First Mortgage was nevertheless a first lien on the entire Extension to the full extent of the \$50,000,000 of First Mortgage bonds outstanding was

rested on that portion of the after-acquired property clause which gives a lien where First Mortgage bonds or their proceeds were used "on account of the purchase, acquisition or construction thereof or work thereon" (R. 122). This was construed as granting a lien for the entire \$50,000,000 on the entire extension if it was financed "in any part" (even \$1,000) "with first-mortgage bonds or cash deposited under that mortgage" (R. 264). This holding is inconsistent with the strict construction of after-acquired property clauses (*Smith v. McCullough*, 104 U. S. 25) and with the doctrine of *pari passu* lien, exemplified by the case of *Citizens Savings and Trust Co. v. Cincinnati and Dayton Traction Co.*, 106 Ohio St. 577.

3. The third lien question relates to non-carrier real estate (R. 1089-91), of a book value of approximately \$1,850,000, which the Refunding Mortgage Trustee contends is free from both the First Mortgage and the Refunding Mortgage, and must be given consideration, as unmortgaged property, in the allocation of securities to the Refunding Mortgage creditors, as well as the First Mortgage creditors, in the event it is found that they are not fully secured.

The Refunding Mortgage Trustee's argument is based on the provisions of the 1915 plan of reorganization of the Debtor's predecessor, which restricted the lien of the First Mortgage to "existing railway properties" (R. 1141), and on the lack of any express reference in the First Mortgage to these very substantial pieces of real estate. We consider the interpretation of the First Mortgage as covering such property to be inconsistent with established rules of construction and also to violate the contract created by the 1915 reorganization agreement (Cf. *American Brake Shoe & Foundry Co. v. New York Railways Co.*, 277 Fed. 261, 271-72—S.D.N.Y.).

4. A fourth lien question was presented to the Circuit Court of Appeals, relating to the amount and type of securities that should be issued to the Refunding Mortgage creditors in recognition of their undisputed first lien on pledged securities of Alameda Belt Line and Central California Traction Company (R. 1042-43), in respect of which no new securities are proposed, under the Plan, to be issued.

The supplemental report of the Commission stated that "the lien on the securities of these two companies has no material value" (R. 315), but it made no specific finding concerning the value of the securities, as required by *Consolidated Rock Products Co. v. DuBois*, 312 U. S. 510, and *In re Chicago, Milwaukee, St. P. & P. R. Co.*, 124 F. (2d) 754 (C.C.A. 7).

Moreover, the record shows that *some* value must be given to these securities, since they carry ownership of important feeder lines, which produce an aggregate of \$500,000 per year of traffic for the Debtor (R. 110, 203, 1312); and the Debtor's Trustees have testified that the benefit derived by the Debtor from its ownership of these lines is greater than any loss it suffers from having to make advances to them (R. 1315; see also R. 1262-63, 1102).

By requiring that the Interstate Commerce Commission find the value of the property subject to the Refunding Mortgage (R. 2670), the Circuit Court of Appeals has paved the way for a proper solution of this question, and it need not be considered further in this Court.

The Circuit Court of Appeals' decision requires, as observed above, that the Commission value the property subject to each mortgage. But an attempt to fix the

values of separate parts of the Debtor's properties, and to make a correct allocation of securities on the basis of such values, will be difficult and wasteful, if not impossible, until there has been a final adjudication concerning the priority of liens on the Debtor's properties.

Therefore it is desirable and necessary that such questions of priority be determined at this time.

Questions presented

The first and fundamental questions presented by this petition are:

1. Should a proceeding be remanded to the Interstate Commerce Commission for determination of the value of the properties subject to the liens of various mortgages without a final adjudication by the Court of legal questions squarely and properly presented to it concerning the extent of the lien of such mortgages?
2. Is it proper for an appellate court, reviewing objections to a reorganization plan, to leave undetermined questions of law, squarely and properly presented to it, affecting the priority of lien on over \$12,000,000 worth of the Debtor's property?

If this Court reviews the whole case on certiorari, the following further questions will be presented to it for determination:

3. Is equipment acquired by a mortgagor with free funds under equipment-trust agreements subject to the lien of the Company's First Mortgage when that Mortgage provides:

"The Company may, unless First Mortgage bonds shall have been authenticated and delivered or their proceeds or other cash deposited here-

under paid out against the same, purchase and acquire equipment, free from the lien hereof, by lease, conditional sale agreement or under any form of equipment trust" (R. 1229)

4. Where less than half the total cost of the Debtor's Northern California Extension was supplied from the proceeds of First Mortgage bonds, and less than half of the cost of the land on which it was built was paid from proceeds of First Mortgage bonds, and the balance (over \$5,000,000) of such cost was furnished by creditors who are pledgees of Refunding Mortgage bonds, is such Northern California Extension subject, under the facts shown in the record, to the exclusive prior lien of the First Mortgage to the extent of the entire \$50,000,000 of First Mortgage bonds outstanding, or is it subject to the First Mortgage only to the extent of the proceeds of First Mortgage bonds used in its construction, and otherwise subject to the *pari passu* lien of the Refunding Mortgage?

5. Is non-carrier real estate which is not described in the First Mortgage nevertheless subject to its lien, particularly when the reorganization plan under which such Mortgage was created restricted its lien to railway properties?

Reasons relied on for the allowance of the writ

1. The Circuit Court of Appeals has decided a federal question respecting the necessity of determining the lien status of property of a company in reorganization, in a way which is in conflict with the decision of this Court in *Consolidated Rock Products Co. v. DuBois*, 312 U. S. 510.

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Determination of the property on which creditors hold liens is fundamental to the enforcement of the absolute or full priority doctrine of *Northern Pacific Ry. Co. v. Boyd*, 228 U. S. 482, and *Case v. Los Angeles Lumber Co.*, 308 U. S. 106, 122. This Court's opinion in *Consolidated Rock Products Co. v. DuBois*, 312 U. S. 510, 520, made that plain at the outset, the Court mentioning not only the necessity of "the requisite valuation data" (312 U. S. 520), but also stating (*ibid.*):

"In the first place, there must be a determination of what assets are subject to the payment of the respective claims. This obvious requirement was not met."

The decision below fails to distinguish between the questions of fact respecting the value of the property subject to the liens of the respective mortgages, and the questions of law concerning what properties are affected by those liens. The former questions may properly be remitted to the Commission for determination in the first instance; the latter questions must be decided by the courts at the earliest opportunity, and the duty to make such decision may not be avoided or postponed.

2. The Circuit Court of Appeals, by failing to decide all the questions before it, has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

The questions concerning the extent of lien were squarely presented to the Circuit Court of Appeals on this appeal. They are set forth in the Refunding Mortgage Trustee's statement of points on its appeal (R. 1652-53). They were fully briefed and argued before the

Circuit Court of Appeals, but its opinion contains not a word relating to such issues, except the statement (124 F. (2d) at 139) that the determination of the value of the property subject to the Refunding Mortgage and the First Mortgage "of course, necessitated a determination as to which of the Debtor's property is, and which is not, subject to each mortgage."

Nothing can be gained but delay by referring these legal questions to the Commission again. The Commission has already made its provisional determination (R. 267) of what property is subject to the Refunding Mortgage, although recognizing (R. 262) that its determination was only preliminary and that final adjudication of such matters must be made by the court. The District Court has already passed on the matter (R. 1597), albeit in a summary fashion.

In the normal and orderly course of procedure, the errors which the Refunding Mortgage Trustee complained of in the action of the Commission and the District Court should have been decided before the case was remanded.

As was stated in *The Bay of Naples* (48 Fed. 737—C.C.A, 2):

"when the law gives a party a right to appeal, he has the right to demand the conscientious judgment of the appellate court on every question in the case."

This Court has held, in reviewing decisions of the old Circuit Courts, that it is reversible error to refuse to make a finding one way or another on a question of fact material to the determination of the cause (*The Francis Wright*, 105 U. S. 381, 387; *Merchants Insurance Co. v. Allen*, 121 U. S. 67, 71). The same principle should apply to the decision of questions of law.

The decision here is also inconsistent with the theory of the ruling of the Circuit Court of Appeals for the Seventh Circuit in *In re Chicago, Milwaukee, St. P. & P. R. Co.*, 124 F. (2d) 754-63, that,

"findings must be made on all vital issues, controverted or uncontroverted, and must include values of property separately considered, and also of Debtor's property as a whole."

Although the *Milwaukee* opinion refers to findings of fact concerning value, it is equally applicable to the necessity of determining what property is to be valued.

As the record now stands, the Commission and the District Court may rule, when the case is remanded, that their prior determinations respecting lien are the law of the case; if so, the first opportunity to correct them will arise when a new plan of reorganization has been adopted by the Commission, approved by the Court, and brought before the Circuit Court of Appeals on a second appeal, many months hence.

All the facts necessary to decide the extent of the lien of the Refunding Mortgage are already in the record. Before being instructed to make findings concerning the value of the property subject to the Refunding Mortgage, the Commission was entitled to the answer of the Circuit Court of Appeals to the legal questions presented by the Refunding Mortgage Trustee's appeal concerning what property is, in point of law, subject to the Refunding Mortgage.

3. This Court has power, if it grants certiorari, to dispose of all questions arising on the record.

Story Parchment Co. v. Paterson Parchment Paper Co., 282 U. S. 555, 567-68;

Donovan v. Pennsylvania Company, 199 U. S. 279, 292;

Delk v. St. Louis & San Francisco R.R., 220 U. S. 580, 588-89.

Although the Court may remand the case to the Circuit Court of Appeals for the decision of questions which the Circuit Court of Appeals erroneously refused to consider (*Liberty Oil Co. v. Condon National Bank*, 260 U. S. 235, 245), such a remand here would inevitably mean a longer delay before the final approval of the Plan than if this Court itself shall decide the lien questions.

In order to carry out the policy of expediting railroad reorganizations (*Continental Illinois National Bank v. Chicago, Rock Island & Pacific Ry.*, 294 U. S. 648, 685), this Court should itself consider and decide the lien questions in conjunction with any other matters of which it shall grant review.

4. Since this petition relates not to error in any rulings by the Circuit Court of Appeals on the lien questions, but only to its refusal to decide them, we deem it unnecessary to present in any further detail the arguments supporting the Refunding Mortgage Trustee's position on questions 3, 4 and 5 above until after certiorari has been granted.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari be issued out of this Court to review the judgment of the United States Circuit Court of Appeals for the Ninth Circuit, dated February 16, 1942, amending on rehearing its order entered November 28, 1941, in respect of the questions mentioned in the above petition concerning the lien of the Refunding Mortgage

on the properties of the Debtor; and that petitioner be granted such other and further relief as to this honorable Court may seem just and proper.

Dated: March 28, 1942.

HAROLD C. MCCOLLOM,

Attorney for Petitioner, Irving Trust Company,
as Successor Trustee under the General and
Refunding Mortgage of The Western Pacific
Railroad Company.

ORRIN G. JUDD,
Of Counsel.